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JOBLESS RECOVERY TIED TO SLUGGISH GDP GROWTH AND LARGE NUMBERS OF PART-TIME WORKERS

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Third-quarter GDP increased by 2 percent but the jobless rate at the end of that quarter (September) was 9.6 percent compared to 9.5 percent at the end of the second quarter (June). Why this apparently counterintuitive outcome? Doesn't an increase in output require additional labor inputs? Are we experiencing a jobless recovery?

Some analysts argue that during a recovery increased production does not yield the hoped-for reduction in the rate of unemployment because large numbers of persons enter labor force hoping to find work. True enough. However, the number of discouraged workers who were not in the labor force because they gave up looking for work increased from 706,000 in September 2009 to 1,209,000 in September 2010.

Another possible reason gains in production can be achieved without additional labor inputs is that employers find ways to utilize their current workforce more productively. Also true enough, but third-quarter 2010 productivity data for the nonfarm business sector are not yet available. And even though there were substantial productivity gains in all four quarters of 2009 and in the first quarter 2010, the annualized rate of output per hour in the second quarter actually slipped by 1.8 percent.

A third possibility as to why increased production has not slashed the jobless rate is the availability of large numbers of persons working part time whose hours can be extended without impacting either the employment or unemployment totals. Private-sector workers in September 2010 worked on average 34.2 hours per week compared to 33.8 in September 2009. Moreover, in September 2010 there 9,472,000 persons working part time for economic reasons. Three years earlier before the recession took hold there were 4,575,000 persons working part time for economic reasons. Additionally, during the 12-month period ending in September 2010 the index of aggregate weekly hours for private nonfarm payrolls increased in both the goods-producing sector and the service sector.

Mayo Research Institute is convinced that this part-time labor force dynamic is an important reason, perhaps the single most important reason, that a third-quarter increase in GDP did not lower the rate of unemployment.

Notwithstanding the economy-wide 2 percent increase in GDP in the third quarter, sluggishness was reported in several important economic sectors including gasoline and other energy goods, financial services and insurance, clothing and footwear, computers and peripheral equipment, and farm inventories. Following a large improvement in the second quarter, purchases of residential structures for rent dropped by 29.1 percent in the third quarter. No doubt some of the workers in these declining sectors became redundant but were not able to take jobs in other sectors that were growing. Is it likely that a jobless construction worker or assembly line worker will meet the requirements for a job in the growing health care sector, especially when unemployment insurance allows them to wait to be re-hired on their old jobs?

The historical record shows clearly that the labor market improves very slowly following a deep recession. To illustrate, the jobless rate in August 1983 was 9.5 percent. It wasn't until July 1997 that it dropped below 5 percent. The current recession for sure is every bit as bad as the recession in the early 1980s. Though it is no comfort to those who are out of work, *a jobless recovery is the norm following a deep recession.*

It's as if the jobless face the same problems as deep-sea divers. The descent to the depths may be very rapid but the ascent to the surface is much slower in order to prevent the bends, to avert another wave of irrational exuberance.

The third-quarter GDP numbers reveal other weaknesses in the U.S. economy. Annualized estimates of imports ($2.404 trillion) vastly exceeded exports ($1.842 trillion) in spite of a weaker dollar which makes U.S. produced goods and services cheaper in international trade. In national income accounting, an excess of imports over exports has a negative effect on GDP holding back the increase for the quarter. In the extreme, if imports were totally eliminated, third-quarter GDP would have increased by 4.61 percent on an annualized basis instead of 2 percent.

Imported goods are a double-edged sword. They are much in favor by U.S. consumers who are attracted to the prices of imports that often are lower than equivalent goods produced in the United States. On the other hand, jobs for U.S. workers are lost when U.S. employers no longer are able to compete against cheaper imported goods.

The underlying sluggishness in the private sector is uncovered when federal government expenditures are removed from estimated GDP. Specifically, third-quarter GDP growth drops from 2.0 percent to 1.29 percent. The huge growth of federal government spending is clearly evident in the percentage point contributions to GDP rising from 0.09 points in 2007 before the current recession started to 0.71 points in third quarter 2010.

A cautionary note. The estimated 2 percent increase in third-quarter GDP, according to the Bureau of Economic Analysis, is "based on source data that are incomplete or subject to further revision." Final estimates for third quarter real GDP will be released at the end of December. Those final estimates, however, are likely to be within a range of 1.9 percent to 2.1

percent.

While admitting that the current recovery may become much more robust in the months ahead, Mayo Research Institute asserts with confidence that it will take years for the job market to return to a much more acceptable 5 percent jobless rate. It just takes a long time to flush out the abuses and ill-gotten gains that led to the financial meltdown in 2008, and put Americans back to work.

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